Report of Alberta Automobile Insurance Board to the Minister of Consumer and Corporate Affairs Respecting the Use or Elimination of Factors of Age, Sex and Marital Status in Automobile Insurance Rating

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INDEX

		Page
I.	Introduction	1
II.	Background	2
	A. Authority of the Automobile Insurance Board	2
	B. Traditional Function of The Board	3
	C. Involvement in Issue of Discrimination	4
	D. Need to Conduct Independent Examination	5
	E. Qualification of Board to Conduct Investigation	6
III.	Purpose of Report	7
IV.	Historical Perspective	7
	A. Description of Traditional Scheme	7
	B. Criticism of Traditional Scheme	11
V.	The Issue	12
VI.	Arguments in Principle	14
	(1) Does the System Produce Equitable Results	15
	(2) What is the Purpose Underlying Human Rights Legislation	19
VII.	Practical Issues	21
VIII.	Mode of Evaluation of Classification System	28
IX.	Analysis	30
X.	Recommendation	40

I. Introduction

The Automobile Insurance Board of Alberta ("the Board") has investigated the issue of the use or elimination of factors of age, sex, or marital status in automobile rating practices utilized by automobile insurers within the province. This report is the result of a review of the discussion which has ensued among interested parties and commentators since the Board of Inquiry Report of 1978; a review of various studies conducted outside of Alberta into the current automobile rating criteria; an examination of alternative rating systems; and a consideration of submissions made by members of the Alberta public respecting the automobile rating system in Alberta.

The investigation was undertaken by the Board in response to a request by the Minister of Consumer and Corporate Affairs following the release of the Board of Inquiry ("the Inquiry") Report of 1978, for advice upon the question of whether automobile insurers should be exempted from the effects of The Individual's Rights Protection Act, or alternatively, whether the use of the factor of sex in automobile rating should be prohibited. The extent of the investigation ultimately undertaken by the Board was much broader than was originally intended, and some explanation of the expansion of the initial task is in order.

We begin with a brief description of the statutory authority of the Board, its traditional function, and its involvement in the issue of illegal discrimination in automobile insurance rating. We then outline the developments monitored by the Board from which the Board apprehended the need to conduct inquiries of its own.

A brief account is given of the considerations of the Board in undertaking the task and finally the purpose of the Board in presenting this report to the Minister of Consumer and Corporate Affairs is stated.

II. Background

A. Authority of the Automobile Insurance Board

The Alberta Automobile Insurance Board is established pursuant to Section 338(1) of The Alberta Insurance Act. The Act requires all insurers to file with the Board schedules of prices to be charged for motor vehicle liability policies ("rates"), schedules of rates for minimum insurance and schedules of classifications of vehicles. The insurer may not change those rates until the change has been approved by the Board. Thereafter, if any insurer seeks to increase its rates or alter any classification, it must apply for and receive approval from the Board to do so.

Section 339 of The Alberta Insurance Act authorizes the Board to investigate any matter it thinks fit respecting automobile insurance in Alberta, including rates, benefits and availability of automobile insurance. It is authorized to prohibit certain rates for minimum insurance, changes in classification of vehicles and changes which, in the result, increase insurance rates for an insured person or class of persons.

B. Traditional Function of the Board

The Board traditionally has perceived its function as that of ensuring to the Alberta motoring public the availability of compulsory insurance at commercially competitive rates. This function has been performed by analyzing statistical data published annually by the Insurance Bureau of Canada ("the Green Book"). With the aid of an independent actuarial consultant, the Board determines whether the projections made from the Green Book's statistics justify changes in the current automobile insurance rates. Such determinations are based on the premise that automobile insurance rates are directly proportional to the frequency and cost of automobile accidents within the jurisdiction.

The Board fulfills its statutory function primarily by its independent examination of proposed rates and changes of vehicle classifications established by automobile insurers. It recognizes its flexibility however, and, in monitoring the industry, has used its authority to make adjustments when needed and where suitable. For example, in 1976 the Board reported to the Government that the residual market for automobile insurance required revision. In 1978, it enlarged its function to include the review of rates given on risks insured by the Facility Association Plan. In 1980, it directed insurers to delete the classification of male drivers aged 25 - 29 and to rate drivers over the age of 25 without regard to sex or marital status.

C. Involvement in Issue of Discrimination

For some years preceding the Inquiry's report, the Board had been aware of complaints from the young male drivers of discrimination in auto insurance rating on the basis of sex. In its annual report dated December, 1977, the Board indicated the receipt of such inquiries, but it took the position that the statistics and actuarial analysis supported differing classifications of risks, notwithstanding that the same might constitute a violation of The Individual's Rights Protection Act.

In a subsequent annual report, the Board confirmed its views that the current classification system used to identify differing degrees of risk was essential to the determination of rates, and it conformed to acceptable actuarial principles and to the practices and experience of automobile insurers carrying on business in Alberta. On September 7, 1979, the Board advised the Minister of Consumer and Corporate Affairs that it considered the existing rating and underwriting practices to be justifiable and defensible. It recommended an exemption as it had done in its annual reports to the Minister delivered in 1977 and 1978, that automobile insurers be exempted from the effects of The Individual's Rights Protection Act in respect of their use of any factors of age, sex, or marital status in automobile insurance rating.

However, shortly after reiterating its view on the issue to the Minister, the Board became aware that in-depth research was to be undertaken in the Province of Ontario into possible alterations to the current automobile rating criteria. Since changes to the current rating criteria would affect rates charged to Alberta motorists, the Board determined that this issue fell within its jurisdiction.

The Board undertook in 1979 to evaluate and report to the Minister upon the results of the Ontario research. The Board thus monitored the progress of the various studies. Because of the uncertainties presented in some of the research and the Board's growing concern during the years between 1979 and 1982 as to the applicability of the Ontario-oriented studies to the case of Alberta, the Board decided that it should undertake its own investigations into the systems of neighbouring jurisdictions purporting to employ auto rating criteria without the use of factors of age, sex, and marital status. Then, in 1984, the Board decided to investigate the attitudes of the Alberta motoring public before it could complete its advice to the Minister. It thus conducted public hearings in Edmonton and Calgary in October and November of 1984.

D. Need to Conduct Independent Examination

The Board's determination that there was a need to undertake some investigation of its own evolved over a period of time and was prompted by a number of factors. One of these factors was that the periodic release of various studies from Ontario apparently had not served to quiet the continuing controversy over the issue in Alberta. Another factor was that attempts between members of the insurance industry and the Alberta Human Rights Commission to attempt to "negotiate" a solution had not produced a consensus.

The fact that the Inquiry's report had called for a further study into the question of whether there should be an exemption to insurers for, or a prohibition of, the use of the impugned factor of sex in automobile insurance rating remained an underlying consideration.

E. Qualification of Board to Conduct Investigation

There were also arguments against the Board conducting its own investigation. One such argument was the fact that the Board, on previous occasions, had expressed its view upon the issue that the current system should be retained. This argument brought the objectivity of the Board into question. An even more critical argument was that such an undertaking effectively required the Board to analyze and pronounce upon the validity of its own modus operandi. Indeed, the Inquiry noted that the Board sanctioned the current rating system in the exercise of its statutory authority and that indirectly through the Board, the Alberta Insurance Act encourages and perpetrates that classification system which gave rise to the illegal discrimination found.

Against these arguments, the Board had to weigh the considerations that the resolution of the issue could affect rates charged to the Alberta motoring public and that the Board had a particular expertise with the practical aspects of the automobile insurance rating system. The Board concluded finally that it had an obligation to offer some detailed advice upon the issue to the Government. However, because of the potential problems in its performing such an analysis, the task would need be circumscribed. Thus, while the Board does relate its investigation to the issue left open by the Inquiry - whether or not auto insurers should be exempted from the effects of The Individual's Rights Protection Act - it does not purport to do so as the government body called for to assemble the appropriate experts to analyse the question.

III. Purpose of Report

The Board's task here is to provide to the Minister of Consumer and Corporate Affairs the results of its study and its recommendation in reference to the question of whether factors of age, sex, and marital status should be excluded in the practices of automobile insurance rate-making by reason of the inability to justify such use in the face of principles of human rights prohibited by and embodied in The Individual's Rights Protection Act of Alberta. It is hoped that the review of the research conducted in Ontario and Alberta might form a convenient compendium of information relevant to the issue to assist the Government in its future deliberations upon this issue.

The Board's aim is to set out the salient arguments in support of each side of the issue, with reference to the studies and submissions presented to Government, to the auto insurance industry and to the Board itself, and to analyze briefly the issue in light of those arguments and to indicate the various courses of action available to the Government. Later, the Board will offer its view of the course of action most advisable from the perspective of the Alberta motoring public.

IV. Historical Perspective

A. Description of Traditional Scheme

A necessary starting point to the task is a brief description of the development of the traditional rating scheme.

It should be said that the scheme developed within an established consultative relationship between government, through the Association of Superintendents of Insurance, and industry. The Association was formed in 1917 and, since that time, has been involved in the drafting of insurance legislation, and the encouragement of uniform practices within the industry. Throughout its history, it has relied heavily on the initiative and expertise of the industry and most innovations are results of extensive consultation with industry representatives.

The present scheme originated in 1926, with the concurrence of government, the insurance industry, and the public. At that time, the Canadian Automobile Underwriters' Association began to gather Canadian auto insurance statistical data. In 1930, a Royal Commission in Ontario investigated the matter of automobile premium rates and concluded that future loss costs should be established by the combination of experience of all companies and that experience should be developed pursuant to the Statistical Plan prescribed by the provincial Insurance Act. The purpose of the Statistical Plan was to define groups of insured persons in such a manner as to provide predictive value for them. The actual losses predicted for each group would be expected to equal the provision for losses made in the rates.

In accordance with the Commission's recommendation, an Automobile Insurance Statistical Agency was appointed for Ontario and other provinces whose insurance legislation contained provisions similar to Section 69(a) of The Ontario Insurance Act. One of those provinces was Alberta. Insurers were required to report automobile premium claims experience and classification

criteria to the Statistical Agency, which was authorized by the Superintendents to amass the information in accordance with the Statistical Plan in a compilation known as The Green Book. Statistics arranged according to class are compiled, collated, and then used to prepare the experience exhibits contained in The Green Book. The experience exhibits express statistical information in a number of forms relevant to the process of predicting the probable cost of insurance rates required to offset expected future losses arising from bodily injury and property damage claims.

The Association of Superintendents of Insurance then created an Auto Statistical Agency Committee which, with the assistance of auto insurers and actuarial consultants, has provided advice for the experience reports since 1940. The original Statistical Plan has been refined considerably over the years since its inception through co-operative efforts of private industry and government officials. Modifications to the Statistical Plan require approval by the Superintendents and take effect in approximately three years.

The requirement for a Statistical Plan and the entire structure of auto insurance rate setting flows from auto insurers collective loss experience compiled within the statistical framework contemplated by statute. The development of the classification is the result of consensual study by insurance, actuarial, industry, and government representatives. Automobile insurers are encouraged, although not legally obliged to establish rates in accordance with the Statistical Plan. Governments have varying supervisory control over the auto insurance rates charged to the public. In some jurisdictions, the Superintendent has the statutory responsibility to be

satisfied with the fairness of the rates, and in other provinces, rating boards have the legal authority to approve or disallow rates.

It would appear that private auto insurers usually examine The Green Book exhibits, perform an actuarial analysis upon certain of that information, together with their own company statistics, and develop a potential for rate adjustment which is then subjected to management and underwriting judgment and analysis.

The first Statistical Plan developed in response to a public demand was thus introduced in 1930. After a decade of use, it contained only two private passenger classes, being business use and pleasure use. The initial statistical groupings have been subdivided over time by the introduction of additional factors, including territory, previous accident claims, age, sex, and marital status. The age factor was introduced to the system in 1950 - 51. The sex factor emerged in 1957 and marital status came into use in 1964. In the system at present, the age factor is employed to separate drivers over age 25 from those under 25, because the former group is said to have a statistically lower risk of accidents and claims. The factors of sex and marital status are employed only in relation to the under age 25 group. Moreover, the factor of marital status is utilized only in relation to the group of under age 25 drivers who are male.

In or about 1977 - 1978, criticisms of the traditional scheme began to emerge. We now turn to a brief description of these developments.

B. Criticism of the Traditional Scheme

In 1978 in Alberta, the Inquiry was established by the Minister of Labour pursuant to Subsection 18(1) of The Individual's Rights Protection Act to investigate complaints against some five insurers alleging discrimination on the basis of sex. The Inquiry was asked to determine whether the insurers practised discrimination contrary to Subsection 3(b) of The Individual's Rights Protection Act.

The Inquiry concluded that in the cases before it, an adverse distinction had been made between the complainant and a member of the opposite sex and the same constituted a violation of the Act. As regards the complaints relating to automobile insurance, the Inquiry noted that new classification systems could be created in the automobile insurance industry in two ways. Firstly, an individual company without long-term statistical experience might propose recognition of a statistically or actuarially homogeneous category, or secondly, a trend to homogeneity might be indicated by statistical data of accumulated experience. The Inquiry concluded that the Alberta Insurance Act encourages and perpetrates the insurance industry classification system which gives rise to discriminatory treatment which violates The Individual's Rights Protection Act.

Elsewhere in Canada, The Ontario Legislature's Select Committee on Company Law in its second report on automobile insurance in 1978 inclined to the view that the current classification system in Ontario was unfair and discriminatory because it charged higher rates to good drivers who were

members of a high-risk class. This concern was compounded because expenses and commissions calculated as a percentage of the higher premium rate were added to the basic charges. The Committee was impressed by the arguments favouring elimination of the factors of age, sex, marital status and urged the industry and the Superintendent of Insurance in Ontario to develop more appropriate alternative criteria.

These events prompted considerable debate between proponents of protection of human rights and defenders of the insurance classification system. Before entering upon an examination of the aspects of the debate, it is well to attempt to define the issue central to it.

V. The Issue

The narrow question is whether the use of the factor of sex in auto insurance rating should be expressly sanctioned by legislation. It is only discrimination on the basis of sex that is prohibited by The Individual's Rights Protection Act and thus some commentators have confined the debate to the sex factor, on the footing that there is no legal prohibition against the use of factors of age and marital status.

If the issue is confined in this manner, the major aspect of the issue is whether and how Government should enact legislation to sanction the use of the sex factor in insurance rating practices. Certain other provinces provide in their human rights statutes a saving provision which permits discriminatory practices if they can be shown to be reasonable and bona fide.

However, the judicial authority in such provinces has rarely, if ever, considered the legal effect of such saving clauses upon the rating practices of auto insurers and therefore there is some doubt whether the enactment of such a saving clause in Alberta would be effective.

The existing legal authority to enact such a saving clause will be thrown further into doubt as of April 17, 1985, by the coming into effect of Section 28 of The Canadian Charter of Rights and Freedoms which provides for a guarantee of equality to male and female persons. This particular section is itself unique within the Charter, in that its effect is not qualified by limitations as can be shown to be reasonable, prescribed by law and demonstrably justifiable in a free and democratic society.

The debate on the sex factor fits within the larger context of the propriety of using as the basis of rating distinctions, the factors of sex, age, marital status, or presumably any other factor which is not within the control of the individual. It is argued that notwithstanding the absence of a specific legal prohibition against the factors of age or marital status, the ethical or philosophical arguments raised against the use of the sex factor apply with equal force to the use of the remaining two factors. Indeed, many of those who argue in defence of the traditional classification system reason that the three impugned factors are used conjunctively and therefore should be considered together rather than in isolation. Thus the broader issue may be expressed as whether any of the factors of age, sex, or marital status should be permitted in auto insurance rating in Alberta having regard to the underlying principles and aims of human rights legislation. This Report deals primarily with the broad rather than narrow scope of the issue.

We now set out a summary of the salient arguments advanced in opposition to and support of the current system. We address firstly the differing philosophical views, and later we examine the debate surrounding the practical means, if any, of altering the current system.

VI. Arguments in Principle

Our starting point in reviewing the essential elements of the debate must be the Inquiry's report. It will be recalled that the Inquiry analyzed the use of the factor of sex in auto insurance rating to determine whether it constituted discrimination within the meaning of The Individual's Rights Protection Act. It concluded that the use did constitute a violation of the Act.

The Inquiry did not agree that changes in classifications were effected to permit groups of drivers with common driving experience to be responsible collectively for costs, rates, and premiums based on that experience. It found the changes were caused by marketing decisions made in competitive industry rather than because of an intention to do equity among homogeneous groups of drivers. The distinction based on sex resulted from market forces, which led to a belief that youthful males had a higher accident rate than females. Such belief was confirmed only subsequently by actuarial and statistical analysis. Moreover, the applicant's risk record was his actuarial experience as a typical member of a class created by gender and by no other test. The Inquiry did not agree that the distinctions based on sex were founded on statistical evidence or that classifications were based on risk.

For the purposes of this Report, we assume the finding that the use of the sex factor in auto insurance rating constitutes discrimination is correct in law. The question raised by the Inquiry's deliberations appears to us as follows. If the use of sex discrimination in auto insurance rating practices violates provincial legislation respecting human rights, but nonetheless accords with and buttresses provincial legislation respecting the supply of auto insurance, how is the conflict to be resolved?

(1) Does the System Produce Equitable Results

The conflict originates with the assessment of the effect of that discrimination which contravenes the statute. The view on one side is that such discrimination is only of a technical form, which when used in the context of the entire system, is not unfair and, in fact, produces equitable results for the majority of the motoring public. The opposing view is that discrimination cannot be qualified as fair or unfair, and in any case, the existing classification system does not produce equity in the result.

The question as to the equity of the results delivered by the traditional classification system may lead to questions of the equity of the results produced by the market and legal framework within which the classification system functions. Considering that a no-fault insurance scheme (VARIPLAN) was proposed in May, 1976, but not adopted in Alberta, it is assumed that for the purposes of this Report, that any changes to be made to the traditional classification would be contemplated within the context of the existing economic and legal framework which is briefly described below.

Insurance services are provided to the insured motoring public in Alberta in the context of the free enterprise system which, in turn, operates within the legal framework of tort liability. Individuals must accept responsibility for their civil wrongs by paying the damages they have caused but they may insure against such responsibility to the extent that the costs can be predicted in advance. Government regulates aspects of these insurance market and legal systems, including the required contents of auto insurance contracts, conduct of business of insurers, insurance agents and brokers, approval of auto insurance rates, age requirements for driver licencing, and penalties for alcohol-related and other driving offences.

As indicated earlier, the proponents of the traditional system say that notwithstanding the technical violation of the statute, the use of the sex factor, as well as the factors of age and marital status, are justified as forming parts of a proper cost-based pricing system. The contrary view is that the current problem is not, but could be, a demonstrably proper cost-based pricing system which accords with fundamental principles of human rights.

We consider firstly the views of the opponents of the traditional system.

a. It is argued that the creation of classifications in the system is arbitrary and unjustifiable and results in a socially offensive stereotype of the young male as a bad driver. Rates and rate increases should not be determined by the immutable characteristics of the driver, but rather by his

driving behavior. The same system has already eliminated or rejected other potentially relevant but socially unacceptable variables. Thus age, sex, and marital status should be eliminated from the rating criteria so as to extend the recognized social limits upon the system.

b. The traditional classification system produces intolerably high degrees of accepted loss variance both within and among rate classes. As it takes a large amount from a small group and reduces only slightly the burden of the many, it is less acceptable than a system which takes a small increment from the many to lighten the load of the few. In short, some drivers are overcharged relative to the risk they bring into the system.

c. Where insurance is compulsory, its availability should not be tied wholly to an ability to pay, because insurance may be a precondition to the operating of a vehicle and in turn to the obtaining of employment.

d. Thus perpetration by the rating system of the stereotype of young, unmarried males as bad drivers can produce compounded negative economic effects. It is unacceptable to take a disproportionate share of costs from those who are economically deprived. Moreover, it is unfair to such high risk drivers to allocate various administrative expenses in proportion to the premium charged.

e. The multiplicative approach in weighing variables such as age and territory yields actuarially unsound premiums for drivers who happen to fall into more than one high-risk category.

f. An additive approach and merit rating plans emphasizing driving experience would better justify the costs of premiums, would be as actuarially sound as the current criteria, would be and be perceived as fairer because the factors would be within the control of the individual and would offer superior incentive effects.

g. Finally, a higher cost of insurance resulting from an elimination of the impugned factors would be a price well justified by the attainment of greater social equity.

Those who support the current system argue as follows.

h. A classification system must be judged from the point when risks are assessed, not after losses are incurred. Thus, rates cannot be assessed on individual characteristics because forecasts of risks can be made only with reference to group characteristics.

i. To extend individual rating to its limit would eliminate the concept of grouping which is essential to insurance. In any case, the introduction of causality and controllability to predict accident experience fails to recognize its randomness. This is reflected in the fact that some current social science theory demonstrates a preference for the use of statistical correlation over causation in the study of social aggregates.

j. Discrimination on the basis of age or marital status does not imply socially offensive stereotypes, and discrimination based on sex taken together

with other factors employed permits the separation of low-risk drivers from the basic classifications. The continuing refinement of the system permits a reduction in rate wherever the improved performance of a particular driving segment including young male drivers is detected.

k. The system will minimize inequitable effects, if it is permitted to employ any factors which are demonstrably valid identifiers of low-risk drivers.

l. It is acknowledged that the current system may result in some adverse effects to young, unmarried male drivers, however, it is expected that eliminating the rating criteria of age, sex, or marital status would result in equally adverse effects to the remaining groups of drivers, and perhaps more serious adverse effects to young, female drivers than currently result to those young, unmarried male drivers.

The foregoing constitutes only a summary of the arguments considered most salient to the issue and does not purport to be exhaustive of all arguments raised on either side of the issue.

(2) What is the Purpose Underlying Human Rights Legislation

The next important aspect of the philosophical debate over the traditional classification system is the question whether, although sex discrimination violates the express wording of the Act, it also runs counter to the underlying aim of the human rights legislation.

Those who say the practice does run counter to the underlying aim of the legislation argue that the legislation is intended to prohibit the perpetration of socially offensive stereotypes and to promote the dignity of the individual. Its principles must apply equally to the conduct of all forms of business and social enterprise in the province.

Those who say the practice does not violate the underlying aim of the legislation argue that the supply of insurance is a necessary social good, yet its concept is inherently discriminatory. It seeks to produce the result where the rate charged most closely approximates the loss cost, which is a striving to minimize unfair discrimination. This view contends that the Act is intended to provide individual members of disadvantaged groups access to fundamental rights relative to employment, education, credit, housing, public accommodation, transportation, and athletics denied to them because of membership in that group, and thus to diminish differentiation which impairs the interest of the individual. The supply of insurance is distinguished from the types of services described above, because the effect of the classification system will not permit a denial of insurance to anyone. This view argues accordingly, that the current classification system does not produce the effects of discrimination the legislation aims to eliminate. If anything, it says that the discrimination which results from the classification system preserves the recognition of differences between persons which results in different treatment which, in general, benefits the interests of the individual.

Those who argue the practice is contrary to the spirit of the Act say in rebuttal that the acknowledgement and extension of this reasoning to

justify discrimination will encourage qualification of the legislation and will promote calls from other groups for similar exemptions. The Act and its underlying principles will be weakened by the acceptance of such reasoning as the aforesaid. It is also argued that this effect was intended to be avoided by the enactment of Section 28 of The Canadian Charter of Rights and Freedoms which is not qualified by Section 1 of the Charter. Section 28 will be invoked after April 17, 1985 in order to prohibit the practice of sex discrimination, because the legislative aim underlying the Charter will be found to accord with the aims underlying The Individual's Rights Protection Act.

Those who argue the practice is not contrary to the spirit of the Act acknowledge the language of Section 28 of The Charter, but urge that its effect will not be fully understood until it has undergone judicial analysis and it would appear likely that even without the statutory requirement that Section 28 be read subject to Section 1, some reasonable qualification to the effect of Section 28 will be found to subsist.

We will consider the arguments concerning the underlying legal and social principles of the two legislative schemes, after a review of the debate over the practical means of effecting change to the current classification scheme.

VII. Practical Issues

The proponents of sexual equality in insurance rating argue as follows. A classification system based upon any of the models in British

Columbia, Saskatchewan, various jurisdictions in the United States, including Hawaii and Massachusetts, the bonus/malus systems in Europe or those seen in South Africa or Rhodesia could be introduced which would not use factors of age, sex, or marital status, yet would still function effectively to supply insurance services to the public. The predictive value of factors of age, sex, and marital status it is said is relatively weak and could be matched or surpassed by variables such as lifestyle, environment, geographic location, miles driven, vehicle use or value, work stresses, driving experience, accident claims history, conviction records, use of restraint and anti-theft systems, tobacco, alcohol and drugs, all of which could be controlled by the individual and would offer an incentive to be a safe driver.

There are differing views about the proper mode of establishing the rate in such a revised system. Some say that all drivers should pay a similar rate initially, which could be decreased or increased based on indicia of improvement or deterioration of driving habits. For example, driver education, vehicle value and clear driving record might justify decreases, whereas driving offences and accidents would cause increases in rates. The incentive aspect would be particularly effective for the young, new driver. Others say that the rate should be made up retroactively when necessary by varying the deductions to rates as individual driving habits emerge.

The proponents for change say that the traditional system should be altered along the lines proposed to eliminate complexity and misunderstanding by the public, and mandatory compliance by insurers should be made a feature.

Those who believe there are no practical means to alter the traditional system in the conventional legal\market framework argue as follows. The elimination of the factors of age, sex, and marital status would require the revamping of classifications, the criteria, the definition of the relationship of the alternative factors, and of all the internal business operations of insurers. It is argued that changes to the Statistical Plan should be developed, controlled, and implemented in sufficient time frames to acquire experience which is credible in an actuarial sense.

It is argued that the industry since 1979 has made sincere and concerted attempts to study alternatives. It has concentrated on variables demonstrably related to claims costs. In the result, some changes have been made to the Statistical Plan effective January of 1985, and include vehicle use by young drivers, the number of years licensed for principal operators licensed less than 10 years, and where there are operators other than a principal one, the driving experience of the operator with least years licensed. The use of these factors will require study before their viability will be known. A proper evaluation will not be capable of completion before 1987. However, if proven viable, it is said that insurers will voluntarily employ such factors in their rating practices. Some argue that the current changes effected since January of 1985 constitute as much refinement to the current system as is possible.

It is further argued that the studies have proven that the surrogate factors are highly imperfectly correlated with expected losses and thus there

are no viable alternative criteria to substitute for age, sex, and marital status.

The reasoning in support of this proposition is as follows. The factors of age, sex, and marital status are concise, inexpensive to establish, relatively stable and easily verified. Age and sex, in particular, are clearly defined, accurate, and consistent over time. Any factor to be introduced into the system must be cost effective. Behavioral variables, by contrast, are expensive to develop, unstable in application, and subject to fraud. For example, mileage as a rating variable is difficult to estimate accurately. Moreover studies as to its validity as a risk predictor surrogate for age, sex, and marital status are inconclusive. A driver's conviction record, although useful, is not suitable as a rating factor because of the varying levels of enforcement, differences in urban and rural regions and difficulties in ascribing proper surcharges applicable. The accident claims record is acknowledged to be valid and is in current use, but is said to have limited predictive value. Similarly, the factor of driving experience is valid and used currently but is thought not a demonstrably valid substitute for age. As for vehicle use, it is admitted to be a valid factor and has been introduced into the system.

The foregoing is said to demonstrate that all behavioral variables that are inexpensive, stable, and verifiable are in current use except where the same cannot be employed in a cost-effective manner.

On the other hand, the elimination of age, sex, and marital status would diminish the certainty and objectivity now present in the system. The goal of achieving the most sound prediction of losses at a price most beneficial to the public as a whole will be attained by a combined use of as many risk factors as are capable of measurement in a cost-effective way. The current rating factors are said to be readily identifiable, the most objective and the most likely to have the greatest effect on risk exposure.

An additional adverse effect predicted by the elimination of the factors is the loss of certain efficiency gains, such as the ability to charge higher rates to clearly identifiable classes of high-risk drivers. Some predict that eliminating these factors would simply produce more subclasses to select against young drivers in any manner not expressly prohibited. It follows that if age, sex, and marital status were eliminated from the rating process, the rates for all age groups would be levelled. Insurance rates for female and more mature drivers would go up, and rates for young male drivers would drop. Insurers would manoeuvre the selection process to attract more of the mature drivers at higher premiums and would avoid the young, new driver at an artificially low premium. In the result, a prohibition effected to eliminate discrimination would, in fact, produce another form of discrimination with the younger male drivers also having to face a difficulty in actually obtaining insurance.

In other words, it is feared that the elimination of age, sex, and marital status may result in the avoidance of risks perceived as underrated, which will increase the population of the residual market and will increase

the rates of lower-risk drivers. Cross-subsidization will result, which effect cannot be sustained over time except by full-scale public regulation of all rates or by public ownership. Although the traditional classification scheme may not produce absolutely correct results, it is said to be the best system attainable within the present market and legal framework.

It is argued that the effect of eliminating factors of age, sex, and marital status is to subsidize young, unmarried male drivers for no valid reason. Studies have established that young, male drivers do pose a greater risk of loss than more experienced drivers, perhaps because of the youthful tendencies of overconfidence, inexperience and exuberance, or perhaps because fewer members of this group are driver trained, and more of them are likely to drive at night and to drive while impaired by alcohol or drugs.

An additional argument is based on the historical evolution of the Statistical Plan. It is said that when drivers were distinguished only by age classifications, it was found that many young drivers were not high risk, and could be insured at a lower rate if they could be identified. It is argued that the factors of sex and marital status were added in an attempt to distinguish sub-groups from the segment of young drivers who had relatively better claims experience than the entire group. Those sub-groups benefited were females and married males. The only means to better ascertain the differences in personality and attitude between those young, unmarried males who have and do not have accidents appears to be via psychometric testing. This method is unlikely to be socially acceptable because it is subjective and constitutes an invasion of privacy.

Even if there are no more effective means of further distinguishing high risk and low risk drivers from the class of young, unmarried males, the proponents argue that insurers continue to attempt to separate the low-risk drivers from that group, by means of discounts for driver training, and academic achievement. It is predicted that the elimination of the factors from the current system would result in a diminishment of service and efficiency in the delivery of insurance to the motoring public.

In answer to those who advert to the bonus/malus and other models of insurance, the proponents of the traditional system say that these models are not viable substitutes for the traditional system because they are neither cost based nor premised on the condition that the expected loss ratio of each class be equal. It is said that these models would not function effectively in a competitive market system. In respect to the suggestion that premiums be calculated retrospectively, it is said that the nature of insurance requires that premiums be collected according to a statistical basis. To decide the premiums after the losses would require the insurer to recover a heavy penalty from those who have claims. Those with such losses would be likely to change insurers or simply to go without insurance, rather than pay the penalties, and thus the remaining drivers would have to absorb such costs.

Still other proponents of the current system argue that the aim of reducing insurance rates for younger drivers could be accomplished without altering the current system if Government would increase enforcement of legislation already in place. In particular, it is argued that loss experience could be reduced by a more stringent enforcement of traffic laws at

night, by restricting youthful drivers' right to drive only during low-risk hours of the day, by reducing the maximum demerit point levels for a license suspension, and by requiring retraining and retesting for a driver who has a claim or conviction during a probationary period.

These philosophical and practical arguments must now be assessed. This task is extremely difficult because there is no consensus as to the proper means of assessment.

VIII. Mode of Evaluation of Classification System

There appears to be no recognized objective standard by which to evaluate the acceptability of any particular classification system. Although there are no codified principles to govern the creation of classifications, discussions among certain North American actuarial bodies have produced a preliminary set of guidelines for discussion purposes within their profession. In view of the relevance of such precepts to the issue at hand, we list below those put forth to date.

1) Grouping of risks is a fundamental necessity of a financially sound system which allows development of equitable insurance premiums which in turn assures the availability of needed coverage to the insuring public;

2) A classification system involves the grouping of risks to determine averages and the application of the averages to individuals;

3) Classification systems should exhibit:

(a) Different classes should exhibit different risk expectations;

(b) Significantly dissimilar risks should be assigned to different classes;

(c) The classes should be large enough to permit credible statistical prediction about that class;

(d) Ambiguity in defining classes should be avoided;

(e) Variables used for classification should be capable of reliable measurement, e.g. age, sex, occupation;

(f) Where possible, the basis for a public perception of a causal relationship between rating factors and classification is desirable;

(g) The system must be acceptable to the public.

The traditional system thus may be tested against these guidelines. Some commentators have suggested that a classification factor should be retained if a reasonable substitute for it cannot be found, and that factors of age, sex, and marital status operate as proxies for some other factors, such as driving experience, social habits, and responsibility. Critics argue that factors of age, sex, and marital status are not supportable because there is no clearly identifiable causal connection between the rating factors and the classifications.

IX. Analysis

There has been substantial study and commentary respecting the validity, if any, of the use of factors of age, sex, and marital status in the insurance rating system. We have attempted to extract from our review of the research, the alternative models and public attitudes, those elements most essential to the question and to set out above the same in a summary form.

We concluded that the research conducted by Ontario groups demonstrates that there are no variables capable of introduction to the system as true surrogates for the factors of age, sex, and marital status. Certain criteria additional to those in current use were found likely to be valid and to improve predictibility of loss experience in current high-risk categories. These were added to the system on January 1, 1985. The actual validity of those additional criteria will be measurable in approximately three years' time.

The next conclusion was that insurance models in the provinces of British Columbia and Saskatchewan function without the use of age, sex, or marital status as rating criteria. It was found, however, that those systems are not cost based and operate in a legal\market framework quite different than that which exists in Alberta. Thus it was determined that unless Alberta was to convert to a no-fault, government-sponsored scheme, none of the features of those models would be applicable to the Alberta scheme.

The public attitudes examined during the Board's public hearings reflected strongly held views, both in support of and in opposition to the use of the factors of age, sex, and marital status in auto rating. Those views in support appeared based on the belief that the current system operated on sound insurance and actuarial principles which delivered the most affordable product possible and thus was as fair a system as was attainable in the context of the Alberta legal\market framework. Those views in opposition persuasively expressed that there was a public perception of unfair treatment to responsible young, male drivers, which effect, since it was in violation of The Individual's Rights Protection Act, should not be countenanced by government, nor indeed, by any government bodies. We now turn to the major aspects of the dispute.

One fundamental area of dispute centres around the proper definition of equity and whether the current system produces equitable results. There appears to us to be no compromise of these opposing views. Perhaps this is because these questions depend, in turn, on the determination of the aims of the human rights legislation in light of the aims of The Insurance Act. If so, the resolution of these questions may ultimately determine whether the aims of these statutes are in conflict or whether they may be reconciled. However, the resolution of these various questions may be a complex task.

On one hand, it would seem that the fundamental legal and civil rights principles governing Alberta society would require that any statutory aim or scheme should be constructed or maintained in a fashion that accords with, rather than derogates from, human rights legislation. If there has been

no compelling argument advanced to date to except the case of insurance from the application of that legislation, then the course of action required should not be in doubt.

On the other hand, a clear preference for the "human rights" view over the "insurance" view is to require substantial alteration of a delivery system of auto insurance services which, in all other respects, operates reasonably effectively and efficiently. The fulfillment of that requirement, unless implemented over a very considerable time period, it is said, will result in palpable market disruption and increased insurance costs to virtually all categories of drivers. If these results obtain, the motoring public is likely to react adversely to the transitional effects felt and additional costs to be absorbed, and to question government and industry about the value of the greater social good attained through such cost and inconvenience. These results may be most disturbing to young, male drivers, some of whom, in the short-term phase following alteration of the system, may find insurance costs anomalously to be even higher than they were in the previous system.

Thus if the predictions of the short-term effects of eliminating age, sex, or marital status criteria are accurate, there is some strength to the argument that the elimination of one or all of these rating factors in order to achieve sexual equality will be a symbolic achievement only, and will not likely produce the effects intended by the enactment of human rights legislation.

It is important in this context, to note that the provisions of the Canadian Charter of Rights and Freedoms appear expressly to prohibit the use of the sex factor in insurance rating as a violation of ss. 15 and 28. Upon a plain reading of these provisions, it is a formidable argument that the use of the sex factor is illegal. However, it may be that the strict application of those provisions will produce an absurd result, that is to say, even greater or similar inequality of treatment of other motorists and if so, one cannot be certain that the judiciary would permit an unqualified effect to be given to such provisions. We are doubtful, accordingly, that the legal effect to be given in these circumstances can be predicted with confidence.

In this regard, we think it unusual that despite relative uniformity generally in insurance legislation within Canada, there appears to be considerable divergence among the various jurisdictions in respect to the use of the sex factor in auto rating. Indeed, the various provincial schemes span the entire spectrum including prohibition of the practice, permitted use if proven reasonable and bona fide, to express statutory exemption. Thus one can discern no clear trend from neighbouring jurisdictions.

We have indicated that the predicted adverse effects of eliminating sex or age or marital status as rating factors are limited to the short term. It seems generally agreed that the effects over the long term are unknown. It is conceivable that competitive business mechanisms, over time, would respond positively in order to restore relative efficiency to an altered system. It is feared, however, that in the long term, greater government regulation might be required in economic and legal matters to ensure conformity with the

classification system after elimination of one or all factors of age, sex, and marital status. Furthermore, there is doubt whether such regulation would be entirely effective to attain compliance with the theory of the scheme. For the purpose of reviewing the most popular proposals for change of the current system, we assume the philosophical questions above discussed are resolved in favour of alteration.

It does seem that one area of consensus between the opposing views concerns the major adverse effect of the current classification system. That is, that all young, unmarried, male drivers are required to pay high rates, and the current scheme does not separate the careful, low-risk drivers from that group. It is said that an acceptable means is not available to effect such separation by the loss indicators in current use. In other words, the problem cannot be solved within the system. One proposed solution contemplates treatment of the main problem resulting from the operation of the system without alteration of the modes of classification. It proceeds from the following reasoning.

It is said that the high rates charged to young drivers are proportionate to the frequency and costs of losses sustained by that group. If those frequencies and costs could be reduced, the rates would fall to more tolerable levels. This view of the problem appears to assume that if those rates were reduced, the effects of sex discrimination in auto rating would be minimized, and there would then not be a significant need to enforce the provisions of human rights legislation strictly against auto insurers.

If that assumption is correct, the solution might be for government to undertake a major role in assisting the reduction of loss experience by enforcing more stringently the highway and motor vehicle laws and regulations. Greater attention to enforcement would result in efficient and reliable separation of the careful and responsible young motorists. It is suggested that this means of attacking the true problem underlying the current classification system is the more appropriate course of action, since it will not disrupt the current mode of delivery of insurance, it will not add expense unfairly to the motoring public and it will render the present system acceptable to the public.

It is also argued that while currently auto insurers are not obliged legally to conform to the Statistical Plan or to any acceptable method of rating, clearly it is found presently to be in their own best interests to do so. If the factors of age, sex and marital status were eliminated, some government regulation, applicable to insurers, might become necessary to ensure compliance with the altered system. However, that kind of regulation might be difficult to enforce, expensive to monitor, and unpopular with the private sector. Thus, more stringent enforcement of highway and motor vehicle laws and regulations is seen to be the option most likely to be successful in treating the problem.

Another proposed solution was that of treating new drivers in the same fashion that is, charging the same rate to all new drivers, until a loss

occurs, and then granting a rebate to drivers who establish a clear, driving record and imposing a surcharge upon those drivers with at-fault claims or convictions. It appears to us that these kinds of innovations would be compatible with a no-fault scheme, but not otherwise with the current classification system. Because the premiums collected generally will go to pay the anticipated losses, there will not be a surplus of premium dollars to form a fund for granting rebates to accident-free drivers. While it would be possible to treat new drivers equally and to grant rebates to accident-free drivers by raising the price of all or nearly all rates charged in order to develop a surplus to pay for losses occurring in respect of underrated risks, or to make return payments to those risks later shown to have been overrated, these innovations would transform the system from one that is cost-based towards one that is no-fault. Once again, the appropriate choice may depend on an evaluation of the social equity produced by a cost-based system as compared to a no-fault system.

In summary, the practical problems involved in correcting the current system are significant and the proposals considered are not free from difficulty. Clearly the issues of principle must be addressed at the outset. These appear to us to be as follows:

1. Does the use of the sex factor in auto rating produce effects intended to be prohibited by The Individual's Rights Protection Act and The Canadian Charter of Rights and Freedoms?

2. In particular, does the use of factors of age, sex, or marital status perpetrate offensive social stereotypes and result in the overcharging of motorists in unacceptable numbers and by intolerable percentages?

3. If the foregoing questions are resolved in the affirmative, will the recognition of the principle of social equity justify the probable adverse short-term results and uncertain long term results?

Whether these questions are answered in the affirmative or the negative, it may be advisable that government formulate and espouse to the public a philosophy of social equity to explain its determination of these questions. If the above questions are answered affirmatively, the policy underlying the determination should assist the public in dealing with the transitional effects of altering the system. It will also assist insurance industry and government representatives by providing a standard by which to assess other existing and proposed future rating criteria.

If the policy reflects the view that the current system does produce intolerable inequities, government might bring about a prohibition of the practice in either of two ways. Firstly, it may be sufficient to indicate to the public that it will not endorse the current practices and to call upon the industry to eliminate the same in as undisruptive but efficient manner as possible. At the same time, it may require the further extension of the current exemption in order to avoid the institution of litigation by aggrieved members of the motoring public during the transitional phase. This course of action might reduce the market dislocation and general inconvenience to the

public in the short term. The alternative course of action is to give effect to the policy of prohibition by express legislative amendment. We would not think this course of action would be necessary to obtain compliance from the insurance industry, given the long history of cooperative consultation between insurers and government for the benefit of the consumer. However, if it became apparent that the first means described did not suffice to attain voluntary compliance, the legislative option might then appear more appropriate.

If the questions are decided in the negative, a philosophy of social equity may assist members of the public in reconciling the aims of The Individual's Rights Protection Act with those of The Insurance Act.

If the policy reflects the view that the current system does not produce intolerable inequities, either in terms of offensive social stereotypes or unreasonable insurance rates, or alternatively, by increased regulation or other means, the inequities can be reduced to tolerable limits, then the government should enact an exemption in favour of auto insurers from the application of The Individual's Rights Protection Act and, if required, enact or upgrade enforcement of highway traffic or motor vehicle legislation. If this course of action is adopted, the apparent conflict between the provincial statutes will be resolved. However, it should be noted that there would then remain open the possibility of a Charter-based challenge of the authority of the Automobile Insurance Board. It would seem prudent to await the challenge, if any, and the judicial determination of the question, before considering whether to disband the Board itself to resolve any remaining legal inconsistencies.

If it is decided that one or all of the rating factors under discussion are unsuitable, it remains to consider what sort of classification system should replace the current scheme. We believe that a clarification of the policies underlying the legislative schemes should assist in pointing the direction towards change or maintenance of the current classification system. Once the priorities are decided, practical methods to recognize those priorities likely will be developed by the joint efforts of the insurance industry in conjunction with government.

A final possible course of action is to take no direct action and leave the resolution of the question of the legality of the rating practices for the Courts. This resolution could come about either by way of reference of an issue to the Court, or by a suit instituted by a private citizen or group.

The merits of this option might depend on the result of the judicial analysis. If the issue was construed narrowly, larger issues surrounding the reconciliation of the aims of the statute might be left undecided by the Courts. Even if, on a reference case, the broad issues were analysed and addressed by the Court, some members of the public might not consider the decision to be of binding effect. Thus if the legal determination did not provide a clear answer to the controversy, the problem would revert to the government for clarification or action.

X. Recommendation

The foregoing sets out the optional courses of action seen by The Automobile Insurance Board as available to government in addressing the issue of retention or elimination of any or all factors of age, sex, and marital status in automobile insurance rating.

We take the view that the resolution of the issue demands evaluation, balancing, and perhaps blending of competing social needs involving some issues which are clearly beyond the jurisdiction of The Automobile Insurance Board.

Given that the responsibility of the Board is confined to the task of ensuring the fairest automobile insurance rates to the motoring public, we can provide only a partial perspective upon the issue. It is recognized that we cannot make a recommendation to the government as to how it might best perform such evaluation, balancing, and blending. Having regard to the parameters of the Board's jurisdiction, we offer the following comments.

We believe that the current classification system is sound in many, if not all respects. We recognize that some members of the motoring public consider it to be lacking in some significant respects, but we were impressed with the quality and quantity of public representations favouring retention of the system in its present form. Although most of those individuals urging retention of the current system had some particular knowledge or experience with the insurance industry, many lacking insurance expertise held the same

view. On the other hand, we were also sympathetic to the view that some aspects of the current system either are, or appear to be, unfair. We recognize that the competing social requirements will have to be reconciled in order to resolve the issue, and accordingly, we recommend that government enunciate a social policy which will express to the public the purposes intended to be served by The Individual's Rights Protection Act and The Insurance Act, and which might operate firstly as a standard by which to evaluate the current system, and secondly, if required, as a blueprint to set out the means of reconstructing the classification system.

While we cannot advise the government what should be contained in such a policy, in its application we would favour an approach which would attempt to preserve as much of the current classification system as is possible and which would bring about such alterations to the system as were found to be necessary in a rational and gradual manner. In this way, we would hope that any transition of the system would take place in such a fashion as to minimize as far as possible, the public confidence in the system, both on the part of Alberta motorists as well as members of the insurance industry. Finally, we would recommend that the implementation of any such policy as may be developed be undertaken in consultation with the Association of Superintendants, members of the insurance industry and consumer representatives.

If so desired, the Automobile Insurance Board would be prepared to monitor such consultations.

All of which is respectfully submitted by
The Automobile Insurance Board.